

Message Text

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PASS TREASURY AND FEDERAL RESERVE BOARD

E.O. 11652: N/A

TAGS: EFIN IN

SUBJECT: ESTABLISHMENT OF RURAL BANKS

SUMMARY: FIVE REGIONAL BANKS WILL BE ESTABLISHED AS OF OCTOBER 2, THUS PARTIALLY IMPLEMENTING ONE ELEMENT OF PRIME MINISTER GANDHI'S 20-POINT ECONOMIC PROGRAM. END SUMMARY.

1. ON SEPTEMBER 25, PRESIDENT FAKHRUDDIN ALI AHMED PROMULGATED AN ORDINANCE SETTING UP REGIONAL RURAL BANKS. INITIALLY, FIVE BANKS WILL BE ESTABLISHED ON OCTOBER 2, MAHATMA GANDHI'S BIRTHDAY. THE GOVERNMENT HAD RECENTLY DECIDED THAT 15 RURAL BANKS SHOULD BE SET UP, IF POSSIBLE, BY OCTOBER 2, 1975 OR BEFORE THE END OF THE YEAR. OVER A PHASED PROGRAM EXTENDING UP TO APRIL 1977, IT IS HOPED TO SET UP, SUBJECT TO CONSTRAINTS ON MANPOWER, 50 SUCH BANKS. AS PART OF MRS. GANDHI'S 20-POINT ECONOMIC PROGRAM A COMMITMENT WAS MADE TO DEVISING ALTERNATIVE AGENCIES TO PROVIDE INSTITUTIONAL CREDIT TO LANDLESS LABORERS, RURAL ARTISANS AND SMALL AND MARGINAL FARMERS WHO OWN

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LESS THAN TWO HECTARES. A MORATORIUM ON RURAL DEBTS,

WHICH IS CURRENTLY BEING IMPLEMENTED AT THE STATE LEVEL, HAS RESULTED IN THE DRYING UP ONF ONE OF THE PROME SOURCES OF RURAL CREDIT, I.E., THAT PROVIDED BY THE LOCAL MONEYLENDER AND THUS IT WAS ESSENTIAL TO ESTABLISH SOME SORT OF CREDIT INSTITUTION TO MEET THE NEEDS OF THE RURAL SECTOR.

2. THE PROPOSED RURAL BANKS WOULD BE "LOCALLY-BASED, RURALLY ORIENTED AND COMMERCIALY ORGANIZED" AND WOULD SUPPLEMENT THE EXISTING INSTITUTIONAL AGENCIES LIKE THE COOPERATIVES AND THE COMMERCIAL BANKS. THE CREDIT COOPERATIVES CURRENTLY IN OPERATION SHOW A CONSIDERABLE REGIONAL UNEVENNESS AND A RESERVE BANK STUDY POINTS OUT WEAKNESSES IN THE STRUCTURE OF THESE INSTITUTIONS DUE TO "MANAGERIAL DEFICIENCIES AND INEFFECTIVE POST CREDIT SUPERVISION AND LOAN RECOVERY." COOPERATIVES HAVE ALSO NOT BEEN ABLE TO MOBILIZE ADEQUATE RESOURCES AS SEEN IN THE CONTINUING LARGE DEPENDENCE ON THE RESERVE BANK FOR REFINANCE. AS TO THE ROLE OF THE COMMERCIAL BANKS, ALTHOUGH DIRECT AGRICULTURAL CREDIT INCREASED TEN-FOLD BETWEEN JUNE 1969 (WHEN THE 14 LARGEST BANKS WERE NATIONALIZED) AND DECEMBER 1974, THE FIGURE STILL ONLY REPRESENTS 6 PERCENT OF TOTAL COMMERCIAL CREDIT. LIMITS ON EXTENDING RURAL CREDIT BY THESE BANKS ALSO STEMS FROM THE HIGH COST OF THEIR OPERATIONS AND PROBLEMS WHICH ARISE FROM THEIR BASIC URBAN ORIENTATION. THE RURAL BRANCHES ARE DEPOSIT CENTERS WHOSE CREDIT/DEPOSIT RATIOS ARE WELL BELOW THE NATIONAL AVERAGE AND HAVE THUS BECOME INSTRUMENTS FOR TRANSMITTING FUNDS FROM WEAKER RURAL AREAS TO THE AFFLUENT URBAN SECTOR. THE TREND NEEDS TO BE REVERSED SO THAT FUNDS MOBILIZED IN RURAL AREAS ARE THEN ALSO DEPLOYED THERE.

3. THE SITES CHOSEN FOR THE FIRST FIVE RURAL BANKS ARE AREAS WHERE THERE ARE FEW COOPERATIVE BANKS AND INCLUDE TWO IN UTTAR PRADESH AND ONE EACH IN HARYANA, RAJASTHAN AND WEST BENGAL. THE PROPOSED BANKS WILL BE SPONSORED BY THE SYNDICATE BANK, MORADABAD, THE STATE BANK OF INDIA, GORAKHPUR; THE UNITED COMMERCIAL BANK, JAIPUR; THE PUNJAB NATIONAL BANK, BHIWANI; AND THE UNITED BANK OF INDIA, MALDAS.

4. THE SHARE CAPITAL OF THE NEW BANKS WILL BE MADE UP OF UNCLASSIFIED

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50 PERCENT FUNDS FROM THE CENTRAL GOVERNMENT, 15 PERCENT FROM THE STATE GOVERNMENT AND 35 PERCENT FROM THE COMMERCIAL BANK SPONSORING THE RURAL BANK.

5. THESE NEW RURAL BANKS, THOUGH BASICALLY COMMERCIAL BANKS, WILL BE DIFFERENT FROM THE EXISTING COMMERCIAL BANKS IN THE FOLLOWING RESPECTS: (A) THEIR AREA OF OPERATION WILL BE LIMITED TO A PARTICULAR REGION COMPRISING ONE OR MORE

DISTRICTS IN ANY STATE; (B) THEY WILL GRANT LOANS AND ADVANCES PARTICULARLY TO SMALL AND MARGINAL FARMERS AND AGRICULTURAL LABORERS AND TO RURAL ARTISANS, SMALL ENTREPRENEURS AND PERSONS OF SMALL MEANS ENGAGED IN TRADE AND OTHER PRODUCTIVE ACTIVITIES IN THE AREA OF OPERATION; (D) THE LENDING RATES OF THE BANKS WILL NOT BE HIGHER THAN THE PREVAILING LENDING RATES OF COOPERATIVE SOCIETIES IN ANY PARTICULAR STATE; (D) THE SALARY STRUCTURE OF THE EMPLOYEES OF THE REGIONAL RURAL BANKS WILL BE PRESCRIBED BY THE CENTRAL GOVERNMENT, HAVING REGARD TO THE SALARY STRUCTURE OF THE EMPLOYEES OF THE STATE GOVERNMENT AND LOCAL AUTHORITIES OF COMPARABLE LEVEL AND STATUS IN THAT AREA OF OPERATION OF THE BANK.

6. COMMENT: WHILE THE GOVERNMENT IS MOVING AHEAD WITH REASONABLE SPEED TO IMPLEMENT THIS RURAL BANK SCHEME, IT WILL TAKE SOME TIME TO SEE IF IT WILL REACH THE RURAL POOR IT IS DESIGNED TO SERVE. STILL TO BE SOLVED IS THE PROBLEM POSED BY LARGE SCALE DEMAND FOR CREDIT BY RURAL POPULATION FOR CONSUMPTION PURPOSES. THIS FIRST STEP IN RURAL CREDIT AREA IS HOWEVER A SIGNIFICANT ELEMENT IN PACKAGE OF REFORMS WHICH INCLUDE LAND CEILING LAWS, MINIMUM WAGE AND RURAL DEBT MORATORIUM. SCHNEIDER

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